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No. 95-1784

In The

Supreme Court of the United States

October Term, 1995

DAVID A. KOSS; FREYA B. KOSS,

Petitioners,

vs.

UNITED STATES OF AMERICA,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Third Circuit

REPLY BRIEF FOR PETITIONERS

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DISCUSSION

Respondent's contentions (Br. 5-8), that petitioners are not entitled to the benefit of the mitigation provisions of the Internal Revenue Code, 26 U.S.C. §§ 1311-1314, because petitioners did not meet the requirements of §§ 1312(7)(A) and 1311(b)(1), are incorrect.

1. With respect to § 1312(7)(A), respondent and the circuit court of appeals, in order to come to their conclusions that petitioners have not met the requirements of this section, have misinterpreted certain words contained in this section and, more importantly, have misinterpreted and changed another word and replaced that word with a word having a meaning different from the word contained in this section.

Initially, respondent and the circuit court failed to differentiate the meaning of the phrase "in respect of" from the phrase "with respect to," both of which phrases appear in the section. The former phrase is used each time in the section in connection with the words "any transaction," whereas the latter phrase is used in the section, and throughout other paragraphs of § 1312(7), in connection with the words " a taxpayer" or the word "whom." It is submitted that the phrase " in respect of" is used to describe a relation to one of many possible transactions on which basis of property depends, whereas the phrase "with respect to" is used to describe a relation to only one, specific taxpayer. It is submitted that if Congress had intended both phrases to describe a relation to only one, specific transaction or to one, specific taxpayer, it would have used the very same phrase in the section in all instances and would not have used two different phrases. Congress used the phrase "in respect of" because, contrary to the contention of respondent and the circuit court, Congress knew that there are many transactions which occur and on which basis of property depends and that a

transaction in which property is acquired is not the only transaction on which the basis of property depends.

More importantly, respondent interprets and changes the word "any" as is contained in § 1312(7)(A) to the word "that" (Br. 6) or to the word "the" (Br. 8), as did the circuit court, in the phrase ". . . and in respect of any transaction on which such basis depends. . . ." These changes are uncalled for and patently incorrect. The ordinary meaning of the word "any," as defined in any dictionary, is " one of more than two" or "one of many." Thus, the section contemplates that there are various, and certainly more that one, transactions on which the basis of property depends, whereas the words "that" and "the" limit the required transaction to only one such possible transaction. The replacement of the word "any" with the words "that" or "the" by the respondent and the circuit court in the instant matter and the circuit court in the case of *O'Brien v. United States*, 766 F.2d 1038, 1042 (7th Cir. 1985), caused the respondent and the circuit court in the instant matter and the circuit court in *O'Brien* to erroneously conclude that there is only one transaction on which basis depends and in which the error to be corrected must occur.

If Congress believed that there is only one transaction on which the basis of property depends and intended to delineate that one transaction as being the transaction in which the property was acquired, as is the contention of the respondent and the circuit court, it could have delineated that transaction in the statute or utilized words in the statute to accomplish this belief and intention. Congress did not do so because it recognized that transactions other than the acquisition transaction influence and determine the basis of property. Such other transactions are those in which the Internal Revenue Code requires that adjustments be made to the original basis of the property, including transactions involving expenditures, receipts, losses or other items properly chargeable to the property, all as is set forth in § 1016(a)(1) of the

Internal Revenue Code, 26 U.S.C. § 1016(a)(1) and Treasury Regulation 1.165-1(c).

The respondent and the circuit court in the instant matter failed to recognize that worthlessness of stock is a transaction on which basis depends because § 1016(a)(1) of the Code requires that the basis of the stock be reduced by the amount of the loss incurred as a result of such worthlessness. The failure of petitioners to recognize the loss on their 1977 tax return is, it is submitted, exactly the type of error which the mitigation provisions of the Code were enacted to permit a taxpayer to correct because the error occurred in a transaction on which basis depends. Respondent's contention, that § 1312(7)(A) does not apply in the instant matter because petitioners took no loss whatever in 1977 and because the Tax Court in 1990 only determined the basis of the stock in 1974 (Br. 7), is without foundation in law. Rather, these facts squarely fit the requirements of § 1312(7)(A).

The words of a statute are to be given their ordinary meaning, unless a contrary intention appears from the words of the statute. *Malat v. Riddell*, 383 U.S. 569 (1965). No such contrary intent appears from the words of the statute in question. The respondent and the circuit court failed to give the words contained in the statute their ordinary meaning and by failing to do so they have incorrectly changed the meaning of § 1312(7)(A) from that meaning intended by Congress.

2. Respondent's contention that the decision of the court of appeals in the instant matter is not in conflict with the decisions of other circuit courts of appeals is incorrect, because respondent has misinterpreted the facts and decisions of the conflicting circuits.

In the cases of *United States v. Rushlight*, 291 F.2d 508 (9th

Cir. 1961); *Chertkof v. United States*, 676 F.2d 984 (4th Cir. 1982); *O'Brien v. United States, supra*, and in the instant matter, the taxpayer attempted to invoke the mitigation provisions of the Internal Revenue Code, in order to correct an error made by the taxpayer, which error occurred in the transaction in which the property was disposed of. In none of the cases did the taxpayer seek to correct an error made in the transaction in which the property was acquired. In each case, the year in which the property was disposed of was closed by the statute of limitations.

In each case a determination of the basis of the property had been made in a year subsequent to the year in which the property was disposed of, but for a year prior to the year in which the property was disposed of. In each case, the determination adopted the position of the Internal Revenue Service as to the basis of the property to the taxpayer for a year prior to the year in which the property was disposed of.

In the three cited cases, the taxpayer, in the disposition transaction, erroneously recognized gain, which error was attributable to the increase in the basis of the property as a result of the subsequent determination. In the instant matter, the taxpayer, in the disposition transaction, erroneously failed to recognize a loss in the amount of $105,600, which error was attributable to the increase in the basis of the stock as a result of the subsequent determination. Both the recognition of gain and the nonrecognition of loss are types of errors which may be corrected under §1312(7)(C) of the Code.

Notwithstanding that the above facts existed in all of the cases, the circuit courts in *Rushlight* and *Chertkof* concluded that the mitigation provisions applied and permitted correction of the error made by the taxpayer in the disposition transaction. However, the circuit courts in *O'Brien* and the instant matter refused to permit the taxpayer to invoke the mitigation

provisions of the Code on the ground set forth in *O'Brien*, that the only transaction on which basis depends is the transaction in which the property was acquired and that only an error made in that acquisition transaction can be corrected. It is submitted that the decisions of the *O'Brien* court and the court in the instant matter are in error and result from those errors made by the courts as set forth in 1. above and 3. below.

3. With respect to § 1311(b)(1), respondent and the circuit court of appeals, in order to come to their conclusions that petitioners have not met the requirements of this section, have failed to give certain words, as contained in this section, their ordinary, clear and explicit sense and have replaced said words with words embodying requirements which are not contained in this section and which requirements are contrary to the explicit words contained in said section.

The respondent and the circuit court, in interpreting the words:

> . . . and the position maintained by the Secretary . . . is inconsistent with the erroneous . . . nonrecognition. . . .

26 U.S.C. § 1311(b)(1), failed to give the words "erroneous nonrecognition" their ordinary, clear and explicit sense. These words clearly mean the erroneous failure to disclose, or failure to identify, or failure to acknowledge [a loss]. The words "erroneous nonrecognition" were simply read out of this section by the respondent and the circuit court.

In place of the words "erroneous nonrecognition", the respondent and the circuit court inserted a requirement that the position maintained by the Secretary (in the proceeding in which basis is determined) must be inconsistent with the position

maintained by the Secretary in the year of the error, or inconsistent with the treatment of the error by the Secretary. Such is not what the statute requires. The plain words of the statute require that the position maintained by the Secretary (in the proceeding in which basis is determined) must be inconsistent with the error of the taxpayer. *United States v. Rushlight, supra* at 518. The statute nowhere requires that the position maintained by the Secretary (in the proceeding in which basis is determined) must be inconsistent with any position maintained by the Secretary in the year of the error, or inconsistent with any treatment of the error by the Secretary.

In the instant matter, the Secretary maintained a position in the prior proceeding in which basis was determined that the Video stock had a basis to the petitioners of $110,000. The petitioners claimed that the basis of the stock was $4,400 and reported the latter amount as ordinary income on their 1974 tax return. In the determination proceeding, the Tax Court adopted the position of the Secretary and determined that the basis of the stock was $110,000, which determination took place in 1990. In 1977, the year in which the petitioners claim that the stock became worthless, they failed to take the loss then known to them in the amount of $4,400 because, as the record shows, they had no income tax to pay in 1977 even without the loss. Thus, the error of the petitioners in 1977 was the nonrecognition of loss in the amount of $105,600, which error was inconsistent with the position maintained by the Secretary in the determination proceeding that the stock had a basis of $110,000. The fact that the Internal Revenue Service had no notice of the loss in any amount is irrelevant to the requirement of inconsistency as required by the plain words of § 1311(b)(1) of the Code. The fact is that petitioners filed a tax return in 1977 which contained an error of nonrecognition of a loss due solely to the basis determination which occurred in 1990, which nonrecognition of loss was inconsistent with the position maintained by the Secretary, and adopted, in the determination proceeding.

CONCLUSION

For the reasons set forth above and for the reasons set forth in petitioners' petition for writ of certiorari, petitioners respectfully request that this Court grant the petition for writ of certiorari.

Respectfully submitted,

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